

No. 9220

In the United States
Circuit Court of Appeals
For the Ninth Circuit 3

UNITED STATES OF AMERICA, acting for and in behalf of the Farm Credit
Administration, *Appellant*,

vs.

J. BURLEIGH, *Appellee*.

Brief of Appellee

Upon appeal from the District Court of the United States for the
District of Oregon

C. L. C. DONAUGH,
United States Attorney,

J. MASON DILLARD,
Assistant United States Attorney,
U. S. Court House, Portland, Oregon,
For Appellant.

BURLEIGH & BURLEIGH,
J. BURLEIGH,
Litch Building, Enterprise, Oregon,

J. BOWERMAN,
Yeon Building, Portland, Oregon,
For Appellee.

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CLERK

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STATEMENT OF FACTS

For brevity, the Federal Intermediate Credit Bank of
Spokane will be herein referred to as "the bank," and the
Agricultural & Livestock Credit Corporation, an Oregon
corporation, with headquarters at Portland, will be here-
in referred to as "the loan company."

The enactment of Public Act. No. 666, 71st Congress,
approved February 14, 1931, amending Public Resolu-
tion 112, approved February 14, 1931 (Def. Ex. 23, R.
5) created a situation which was immediately turned to

advantage by the loan company and the bank acting in conjunction with those officials and loan agencies working under the direction of the Secretary of Agriculture. Included in this exhibit, as a part thereof, is an instrument entitled "Preliminary Instructions" (R. 351) and bears date February 26, 1931.

On March 19, 1931, the loan company, through its Vice President, Mr. Will T. Wright, wrote a letter to the defendant Burleigh (Def. Ex. 11, R. 172). The entire letter is important, but in view of certain other portions of the record in this case the following features are deemed of sufficient importance to attract special attention:

"The Federal Intermediate Credit Banks, as you know, are authorized to discount acceptable loans from livestock loan companies to ten times the amount of actual cash capital; therefore, loan companies could expand their loans \$10.00 to each \$1.00 put into new stock. (R. 172-173) The money the Government will advance to increase our capital will enable us further to serve the stockmen in our territory. No provision, however, is made for loan companies to borrow direct. Therefore, we must have your cooperation as a stockholder if we secure the advantages of this opportunity, and if the Government will not advance the full par value of the stock we will accept no cash from our present customers for the amount of the difference." (Oregon law permits the sale of stock by an Oregon corporation only for cash, or something equal to par value, *McAllister v. Amer. Hosp. Ass'n.*, 62 Or. 530, 533, 534).

"Our plan is to offer 6% cumulative preferred stock, which is subject to redemption after two years

from date of issue. We suggest that each of our borrowers own our stock to at least 10% of the amount of the loans we carry, and that he apply for the maximum advance the Government will make on the stock. After two years, if the borrower has paid the loans we have made him, and the Government has made no provision for further extension for repayment of the advance on the stock, we will then redeem the stock at par.

“The stock is preferred both as to dividends and in liquidation over common stock, and the owner of preferred stock is protected against loss by \$40,000.00 common stock and surplus.” (R. 173) * * *

“While we are suggesting that our borrowers take 10% of the amount of their livestock loan of our 6% preferred stock, a larger amount would appear to be decidedly to your interest. If the Government will furnish the funds, at 3½% on the stock paying cumulative 6% dividends, you will make a profit on a well protected stock without putting up any money. At the same time you are assisting in financing the livestock industry. * * *

“We naturally expect support from those whom we are serving, and, in turn, our first obligation will be to our stockholders. Before offering any of our stock to others, we wish to learn first what amount can be placed with those who know us and our methods of doing business.” (R. 174)

“In order that we may be in a position to know at the earliest possible date what amount of stock our borrowers will buy, we will thank you to sign and return to us the enclosed commitment. On the basis of 10% of your present loan, you should own \$300.00 par value, or 3 shares of stock, but as already stated, it will be decidedly to your interest to own a larger amount.” (R. 175)

That a renewal of this note and others like it was anticipated is indicated by the following from the Secretary of Agriculture in defendant's Exhibit 23 (R. 358):

"At the expiration of one year, renewal of the note for a second year will be considered upon conditions then existing, but no loan will be extended beyond the second year."

and in the letter from the loan company to Burleigh (Ex. 11, R. 172):

"These advances will be for not to exceed two years with interest at $3\frac{1}{2}\%$ "

The financial statement of Mr. Burleigh submitted in connection with this loan (Pl. Ex. 4, R. 147) should also indicate to a person experienced in examining credits and lending money that nothing short of a miracle would have made it possible for Mr. Burleigh to pay the original note within one year from any of his own resources. This would seem to be well authenticated by his own financial statement, which presumably was considered in connection with the approval of his loan application. We refer to the following, which shows:

A total indebtedness of.....	\$13,850.00, and
a net worth of.....	12,405.00.

Of his net worth \$7405 is made up of livestock covered

y a first mortgage in favor of the bank for \$3000, and a second mortgage in favor of Wendell Burleigh for \$2000 (R. 152).

The \$3000 first mortgage loan is one of the loans criticized by the examiners of the bank (R. 217) and is classified as "fair."

Among the cattle included are beef cows valued at \$30 per head, whereas W. E. Meyer, Manager of the bank, in his letter to the loan company of May 11, 1931, (R. 212) gave his ideas of loan value on range cattle as follows:

"Your range cattle loans are in general in excess of \$30 per head and some in excess of \$35 per head. It is desirable to reduce these loans in line with present market conditions."

This financial statement also shows (R. 151) that among Mr. Burleigh's liabilities is a note for \$1000 to John Curry, past due from June 1, 1928, secured by a cattle mortgage on Mr. Burleigh's library; that his agricultural and range real estate is incumbered, likewise his dwelling house, and that in addition to his direct liabilities he is obligated for \$1050 as an endorser on notes or mortgages (R. 152).

Before Mr. Burleigh had answered the letter from the loan company, Mr. Wright, its Vice-President and Sec-

retary, made a trip through the country and called on Mr. Burleigh to urge him to buy the company's "A preferred stock (R. 175). Mr. Burleigh had known Mr. Wright for forty years as a banker in the county adjoining that of Burleigh's residence, and as a bank examiner, and knew him as having a good reputation. He had done business with the loan company for a year or two. On this visit Mr. Wright told Mr. Burleigh (R. 176) of the act of Congress and of the need to increase the capital of the loan company in order to enlarge their business and to take care of the needs of the borrowers. Mr. Wright told Mr. Burleigh that if they sold this stock the loan company would take on new loans to accommodate other stockmen needing assistance, and if the present borrowers would take stock so they could increase their capital, it would enable them to serve a greater number of stockmen and to serve their present borrowers to better advantage, and that the purchasers would make money; that this stock proposed to be sold was preferred stock which guaranteed 6% dividends; that the money borrowed would cost 3½%, leaving a spread of 2½%, and that Wright guaranteed that the company would pay the interest on the notes,—“the note that I was to give, and at the end of two years if the government didn't extend the time longer that this company would pay the note” and that he Burleigh would never have anything to pay, either interest or principal. If his loan was extended

yond two years that at the end of the extended period the company would still pay the note. (R. 177-178)

Mr. Burleigh further testified that Mr. Wright told him that the loan company was in sound condition, the stock was worth one hundred cents on the dollar; "and to convince me of that he told me that the Secretary of Agriculture would take the stock as collateral security and loan one hundred cents on the dollar and that is all the security that would have to be put up, would be the certificates for the capital stock of this company."

Mr. Burleigh further testified that on June 5, 1932, when he signed the renewal note (Ex. 1) he had not learned anything more about the business of the company, or anything to cause him to doubt the statements made by Mr. Wright; that he did not examine, nor have an opportunity to examine the books or affairs of the company. He testified that about the time Exhibit 1 was signed, he was asked to sign the renewal note, which was in accordance with his understanding when the first note was given. He said (R. 178):

"Mr. Wright told me that that was the program; that they would make at least one renewal; and when the year was up they asked for a renewal, and I hadn't been asked to pay any interest and I assumed that the company was doing as it said it would do and paying the interest, and I renewed."

Mr. Burleigh further testified that he had never paid any interest on the note and that the renewal note was for the same amount as the original note. He testified that until during the five months preceding the date of the trial he had not learned that the statements made by Mr. Wright were untrue, and that during the five months preceding the trial he had learned of the untruth of the material statements from an examination of the books and the files and records of the loan company; that the management of the company had changed in January preceding the trial, when he and other persons giving notes under circumstances similar to those under which Burleigh signed his note, met in Portland to try to have the loan company keep its promise to protect them from having to pay these notes, and that under threat of litigation in court an application for receivership, and a reorganization was effected following which the records of the corporation became available. (R. 180)

He testified that from an examination of the corporate records and particularly the criticisms from the bank he learned that the stock was practically valueless at the time it was sold to him, and this information came to his hands the first of that year (1938). (R. 181)

Exhibit 1 (R. 124) is the renewal note. The original note was procured from the President of the loan company during the trial in court (R. 164) and appears in Def. Ex. 10 (R. 165).

The federal funds provided under Public Act 666 were available for loans to assist livestock and agricultural loan companies by the purchase of their stock as follows:

- (1) In forming new loan companies;
- (2) (a) To form part of the capital structure of the corporation;
- (b) To expand its capital; or
- (c) To replace any impairment of the capital structure. (R. 354).

Mr. Burleigh made application for a loan for the purpose of increasing the capital stock of the Agricultural Livestock Credit Corporation of Portland, Oregon, (R. 128).

In this respect the representations made by Mr. Wright orally and in his letter, both above referred to, are in accordance with the application, to wit: that Mr. Burleigh proposed to borrow this money and buy stock in the loan company in order to increase its capital and thereby increase its ability to serve the livestock industry generally and its borrowers in particular, at the rate of \$10 for one as above shown.

Attached to defendant's second amended answer (R. 10) is a list of livestock men who purchased similar stock

of the loan company under circumstances similar to those under which the defendant purchased his stock. This loan is identified by Mr. Burleigh in his testimony (R. 180)

That the loan company was enabled to and did sell its stock in accordance with the plan outlined by the bank, loan company, and various representatives of the Secretary of Agriculture to the extent of \$34,700, or 37 shares of the "A" preferred stock, is evidenced by the testimony of John M. Warren, President of the loan company, and formerly an examiner and auditor of the bank. (R. 247-248)

Taken together with the letters of W. E. Meyer, Manager of the bank, which letters were introduced in evidence as Def. Ex. 17 (R. 249-252) the identity and representative capacity of Mr. Altermatt is established and will be hereinafter further identified from the record.

The financial statements of the loan company for the period from March 31, 1931, to and including October 1, 1931, are in evidence as Def. Ex. 20. (R. 286-295)

In order to tie the pertinent portions of two exhibits together, we quote the following: In his letter of June 5, 1931, Mr. W. E. Meyer, Manager of the bank, wrote to Curtice H. Martin, President of the loan company, and enclosed him a copy of Mr. Meyer's letter to Mr. A. B. Altermatt at Shaniko Oregon, which letter to Mr. Altermatt is also dated June 15, 1931. In this letter Mr. Meyer says:

"We are in receipt of your letter of June 13 enclosing the following checks from the Treasurer of the United States representing loans to the individuals listed hereon, the proceeds of which have been used to purchase stock in the Agricultural & Livestock Credit Corporation, Portland, Oregon:" (R. 249-250) (Mr. Burleigh and his check are included in the list).

In the financial statement of the loan company dated March 31, 1931, there is shown to be outstanding:

Capital Stock—Preferred "A"....	\$50,000.00
Preferred "B"....	32,750.00
Common	14,900.00 (R.287)

In the financial statement of the loan company for April 30 (R. 288) the capital set-up is given as follows:

Capital Stock—Preferred "A"....	\$50,000.00
Preferred "B"....	40,250.00
Common	14,900.00

In the financial statement of the loan company for May 29, 1931, the capital set-up is shown to be identical to that of the last preceding one (R. 290).

In the financial statement of the loan company for June 30, 1931, no change is shown (R. 291). No change is shown in the statement for August 31, (R. 293), nor is any change shown in the statement for September 30 (R. 294), nor for October 31 (R. 295).

Restating this matter briefly: the bank at Spokan received checks properly endorsed, amounting to \$34,700 and returned two checks to the agent of the Secretary of Agriculture, Mr. Altermatt, for his endorsement as attorney-in-fact for the borrowers, which, when endorsed, would make up the above total. According to all of the evidence this money was procured from the Treasury of the United States upon supposed loans by the Secretary of Agriculture to various persons, including Mr. Burleigh, the loans having "been used to purchase stock of the Agricultural & Livestock Credit Corporation at Poland, Oregon." The money was received on or about June 15, 1931, by the bank, and from that time on there was no change in the capital stock structure of the loan company, and therefore the supposed benefit of having the capital of the loan company increased by the method adopted by the Secretary of Agriculture, the loan company and the bank was never accomplished, or made available to anyone.

During this entire period the class "A" stock, which Burleigh and the other new stockholders were supposed to buy, never changed from \$50,000. The 8% "B" stock did change from \$32,750 in March, 1931, (the last statement prior to the time this stock was sold) to \$40,250 at the end of April, 1931, but during this period, as will hereinafter appear, the capital structure was reduced by charges against the items reserved for "Losses and Surplus."

plus" in an amount greater than the increase of the outstanding "B" stock, so that when the entire transaction was completed and the Secretary of Agriculture had contributed \$34,700 through supposed loans to various defunct borrowers, the capital structure of the company was less than it was at the end of March, before anything was done.

Throwing a sidelight on these transactions are minutes of the directors' meeting of the loan company held during this critical period. We refer to defendant's Ex. 25 (R. 389) in which we find that:

"He (the President) also stated that some of the owners of Class "A" Preferred Stock of this corporation had expressed their willingness to sell said stock to the corporation at \$75 a share, and use the proceeds to purchase Class "B" Preferred Stock at par."

Upon motion, authority was given to carry such transactions into effect. (R. 390)

It is then set out that:

"The President stated that the Portland Livestock Company, Inc., had proposed to sell to this corporation one hundred (100) shares of Class "A" Preferred Stock at \$75 per share, providing the corporation would credit the obligations it held against the Portland Livestock Company, Inc., \$7500."

Authority for this transaction was given by motion.

It is further stated in these minutes:

“On motion duly seconded and passed, the secretary was directed to carry all Class “A” stock owned by this corporation, or hereafter acquired, as an asset at the par value thereof, and to credit “Reserve for Losses” the discount realized on purchase of said Class “A” stock.” (R. 390)

The following from these minutes would seem to tie this entire stock manipulation to the transaction with Burleigh, and others similarly situated:

“On motion duly seconded and passed, the officers of this corporation were authorized to sell at par Class “A” Stock, which has or may be purchased, to individuals applying for loans under the provisions of Public Resolution No. 666 and to issue said stock prior to the payment therefor, for the purpose of completing the loan, provided, however, that in the event an acceptable loan is not made by the Government, the stock shall be returned to the treasury of this corporation.” (R. 391)

The above explains the only change in the capital stock status of the loan company during the entire period. The amount of outstanding “A” preferred stock never changed. The amount of “B” preferred stock changed from \$32,750 on March 31 to \$40,250, which is exactly the amount of change which occurred as a result of the

Portland Livestock Company, Inc. surrendering 100 shares of "A" preferred stock as a credit for \$7500 on its indebtedness. Just how this \$7500.00 got to be 8% stock, or who got that stock, is not immediately discernible, but it is obvious that the "A" preferred stock, the kind purchased by the newcomers like Burleigh, remained at \$50,000 through the whole period, and no effect was ever given to the \$34,700 of "A" preferred stock which was sold between April 13, 1931, and June 15, 1931, when the money came into the hands of the bank or an equivalent amount of "A" preferred stock. At this time there was \$50,000 of unsold "A" stock, but the lenders sold none of that, but turned in their own stock for the purpose of supplying Mr. Burleigh and others similarly situated, as is particularly provided in the minutes of the directors' meeting of April 13, 1931. (R. 391)

Therefore, instead of this being a loan and increasing the capital of the loan company, as specified in Burleigh's application (R. 128) it turned out to be just a method of repairing the impaired capital of the loan company for the benefit of the loan company and the plaintiff, through his interest in the bank, as will hereinafter appear.

The distressed financial condition of the loan company, and its impairment of capital dates back to the origin of the company and the method adopted in paying for the stock of the company at the time it was originally

issued, which appears in detail in Ex. 25. (R. 381-387)

The outstanding vice in the capital structure of the loan company, which was introduced at this first meeting, originated in the payment by the W. H. Curtice Estate for 2600 shares of common stock, 507 shares of Class "A" Preferred stock and 23 shares of Class "B" Preferred stock. The result of this initial error, with the accumulation of additional losses are in this record to the extent which was thought to be sufficient to demonstrate the extent of the capital impairment at the time of the original Burleigh transaction.

Mr. Burleigh's original note was dated April 1, 1931 (R. 165). Exhibit 12 (R. 208) is a letter dated May 11, 1931, from W. E. Meyer, Manager of the bank, addressed to the directors of the loan company, following which is Ex. 13 (R. 214-220) which is the report of the examiners of the bank of the condition of the loan company as of April 25, 1931.

This letter, and the examiner's report therein referred to, were selected and introduced, as they disclosed the condition of the company as viewed by the plaintiff through its agent the bank, at the very time this stock was being sold to Burleigh and others. The following from Mr. Meyer's letter would seem to be particularly pertinent: (R. 209)

"Your capital, surplus, undivided profits and r

serve accounts amount to—\$98,843.31. The bank cannot consider the following items as a part of your capital as they are non-liquid in character and are of doubtful value

John Hartles	\$ 6,205.14
Curtice Farms, Inc.	36,797.28
Max Schmidt	3,933.31
Real Estate Owned	4,000.00
	<hr/>
Total	50,935.73
Net unimpaired capital and surplus....	47,907.58.”

It is interesting to read the above from the government's agency at Spokane in connection with the letter of Mr. Wright of the loan company to Mr. Burleigh dated March 19, 1931, especially those portions thereof wherein the stock is represented as insuring a profit on a well-protected stock, without putting up any money, and that it would be decidedly to Burleigh's interest to purchase an amount larger than 10% of his loan. (R. 174-75)

Mr. Meyer further criticizes the condition of the company as follows: (R. 209)

“In addition to the foregoing, the following items are undesirable:

Portland Livestock Co. Note.....	\$18,000.00
Portland Livestock Co. Open Acct.....	744.38
	<hr/>
Total	18,744.38

Florence H. Curtice	1,025.00
Total	19,769.38
Items already deducted from capital.....	50,935.72
Total items undesirable (not discounted)....	70,705.10

“The bank’s examiners have frequently discussed these accounts with your officers and you are fully aware of their undesirable features.

“The bank wishes to be advised in detail as to your program for the elimination of each of these accounts from your assets. Losses which have developed or are anticipated should be charged off.”

Mr. Meyer then called attention (R. 211) to six loans which were in excess of the legal limits to the extent of \$39,585.80. It is interesting to note that the S-Bar Land & Livestock Co., which is criticized, and its relatives grew so that at the time of the trial it amounted to \$90,000 with an assured loss of from \$25,000 to \$30,000.

Mr. Meyer told the loan company that:

“We shall be unable to consider new business from your corporation until after you have placed your capital accounts on a more satisfactory basis and have established a proper reserve for contingencies.” (R. 212)

This letter was written May 11, 1931, (R. 208) almost a month after Mr. Burleigh had signed his first note. (R. 165)

Details of criticized loans appear in a column headed "Remarks" (R. 214-220). It is noted that Mr. Burleigh's livestock loan of \$3000, secured by a first mortgage, is included in the list of criticized loans (R. 217). As to the 45 Ranch Company, it will be noted under "Remarks" (R. 218) that this company belongs to Sam Ross, Curtice Martin and Will T. Wright. At this time Mr. Martin was President and Mr. Wright was Vice-President and Secretary of the loan company.

Criticism of mortgage on Curtice Farms, Inc., is found under "Remarks." (R. 219)

The basis for criticisms of the Florence H. Curtice note of \$1025, and of the objections to the real estate owned by the company are found under "Remarks." (R. 220)

After the new money had come into the hands of the company on June 15, 1931, (R. 249-252) at a meeting held June 22, 1931, (R. 391) the directors gave consideration to the bank's criticisms of the company's affairs. As to Curtice Farms \$11,174.45 was charged to Profit and Loss; as to the Max Schmidt loan \$1933.33 was charged to Profit and Loss; as to the real estate owned by the company \$2000 was charged to Profit and Loss,

making a total of \$15,107.79 charged to Profit and Loss (R. 392, 393, 394) one week after the money from Burleigh and other stock purchasers had gotten into the hands of the bank.

In this connection it is interesting to note from these minutes:

“The secretary reported that \$10,950 had been realized through exchange of Class “A” Preferred Stock for Class “B” Preferred, which amount was credited to Reserve for Losses.

“It appearing that the items charged to Profit and Loss are in excess of said reserve, on motion duly seconded and passed, it was ordered that Profit and Loss account be credited \$14,950, and that \$10,950 be charged to Reserve for Losses and \$4000 be charged to *to* Surplus.

“The Board carefully reviewed all of the items listed in examiner’s schedule, and the comments thereon. It was the unanimous desire of the Board that all the matters referred to by examiners be adjusted as speedily as possible, and that the business of this corporation be conducted in a manner to conform to the requirements of the Federal Intermediate Credit Bank.” (R. 394)

Should there be any doubt as to the identity of the Class “A” preferred stock sold to Burleigh and the other similarly situated it is set out in the minutes of the directors’ meeting held January 12, 1932 (R. 394-395) from which we quote:

“The Secretary reported that under resolution authorizing purchase of Class “A” Preferred Stock at \$75 per share, the holders of such stock have sold this corporation 290 shares, and that all of such shares, together with 100 shares accepted from the Portland Livestock Company, and 40 shares heretofore purchased, have been sold at par to persons securing loans from the United States Department of Agriculture.”

The Curtice Farms, Inc., again came forward at this meeting of the directors (R. 396-397) as follows:

“The secretary read proposal from Curtice Farm, Inc., to sell and convey to this corporation all of the property of said Curtice Farm, Inc., subject to existing liens, in settlement of all indebtedness now due this corporation.”

This proposal was accepted (R. 397) and an additional \$449.30 was charged to Profit and Loss.

The affairs of Enterprise Livestock Co., which were criticized in the examination of April 25, 1931, (R. 214) came up for consideration at this meeting on January 12, 1932, at which time it was estimated there would be a loss in excess of \$2000.

The Max Schmidt matter came before the board due to default in interest on his \$2000 mortgage, and the secretary also reported that:

“Information had been received that the Jackson County lands had been sold for delinquent taxes.”

Thereupon the above items were charged to Profit and Loss, and another \$3000 was transferred from Surplus to Profit and Loss account. (R. 398-399)

These items, as above indicated, were all under criticism at the very time that stock of other stockholders of the loan company was being sold to Burleigh and others like him.

The proposal of Curtice Farms, Inc., to turn over its property to the loan company is of interest and appears in the record (399-401). In this connection it will be noted “that the same interests controlled Curtice Farms, Inc., as controlled the loan company.”

In the minutes of a directors' meeting held September 19, 1933, the winding up of the affairs between the Portland Livestock Company and the loan company were provided for and provision made for, the future determination of the loss which would be sustained on this account. (R. 409)

Attention is called to defendant's Ex. 16 (R. 208) dated May 16, 1931, in which Mr. Meyer, Manager of the bank, after a conference with Mr. Wright, apparently relented with regard to the charge-offs ordered in his letter of May 11, 1931 (R. 208). However, under de

of December 4, 1931 (R. 227), Mr. Matson, Assistant Manager of the bank, addressed a letter to the loan company respecting an examination of the loan company made October 29, 1931. The criticisms of examiners in connection with this report appear on pages 233-239. In his letter, the bank, through its Assistant Manager, says:

“Doubtful and loss paper under loans aggregates \$35,473.14.

“In addition you are carrying an open account for the Curtice Farms in the amount of \$15,365.28 of which \$11,365.28 has been classified as doubtful. Real estate taken over in settlement of the Dunn and Sexton loan in the amount of \$2000 has been classified as doubtful. Total doubtful and loss paper on the date of examination aggregated \$48,838.42, which when deducted from your capital, surplus, and undivided profits of \$121,040.51 places your net unimpaired capital and surplus of your corporation at \$72,202.09.

“The bank can only consider discounts on the basis of your net unimpaired capital and surplus. Rediscounts as of this date are in the amount of \$706,000 which is 9.8 times your net unimpaired capital and surplus. This does not take into consideration other liabilities of your corporation.” (R. 228)

“Aside from doubtful and loss paper under rediscounts you are carrying in capital investments \$37,365.28 worthless paper as follows:

Curtice Farms & Schmidt (R/E mortgages)	\$24,000.00
Curtice Farms (Open Account)	11,365.28
Real Estate (Dunn and Sexton)	2,000.00
Total	<u>37,365.28</u>

“We have repeatedly asked that these loans and accounts be eliminated from your corporation’s assets. It is requested that you prepare charge off schedules on these items after which they should be kept in a separate ledger and handled similar to charge offs on rediscounts.” (R. 229)

Criticism was then made of the Portland Livestock Co. and Mrs. Florence H. Curtice loans. (R. 230)

“* * * Directors meetings are not being held regularly and your minute book discloses that only one meeting was held since the previous examination.” (R. 231)

Reverting back to defendant Ex. 16 (R. 241) the letter of May 16, 1931, from W. E. Meyer, Manager of the bank, to Mr. Wright, secretary of the loan company, it will be noted it is therein stated that the capital of the loan company is \$62,150 as of April 25, 1931, whereas the financial statement for March 31 shows a capital of \$97,650, and the financial statement of April 30, 1931, after the Portland Livestock Company’s ten thousand shares of Class “A” stock had been surrendered on credit on the account, shows a capital of \$107,400.

We have called attention to these discrepancies, as the statement at the beginning of April and the end of April are so out of line with what the bank found the capital to be on April 25, 1931.

Concerning the various sour items carried as assets at the time they proposed to sell stock to Mr. Burleigh and others, Mr. Warren (at the time of the trial President of the loan company) testified (R. 262) as to the Portland Livestock Company, which was liquidated, the loan company took back the 3700 shares of its common stock held by the Portland Livestock Company, and that the value of this stock was negligible, if any (R. 263); as to the Forty-five Ranch Company (R. 263) he testified (R. 264) that its property had been sold to Florence Ross; that his property became a part of the property of the S-Bar Land & Livestock Company, and that of the loan outstanding at the time of the stock sale to Burleigh \$25,000 was criticized, and that at the time of the trial the loan had grown to \$90,000. He further testified the loan could not be liquidated and the amount recovered; that a loss was imminent, which he estimated at \$30,000 or more; that the original \$25,000 loan to the Forty-five Ranch Company was a part of the present indebtedness, and that the indebtedness of \$38,700 was the remainder. He testified that these loans, with \$20,000 additional, had now grown into a loss of \$30,000.

Defendant's Ex. 21 contains a list of the losses charged off after the Burleigh stock transaction. (R. 310-315)

The above extended statement of the facts surrounding the affairs of the loan company and its relationship to the plaintiff's agent, the bank, has been set out at length,

before entering upon a recital of the exact circumstance under which the so-called loan was consummated. The plan for consummating the loan is fully set out in defendant's Exs. 23 and 24. (R. 345 and R. 366)

In explaining the procedure for selling stock in a loan company, such as the loan company in this case, the Secretary of Agriculture has this to say, concerning the plaintiff's agent, the bank:

"The Federal intermediate credit system which discounts the notes of such corporations, can accept only such paper as is described in the law governing their operations. That system is not an emergency institution. It is a permanent organization which like any other banking system must protect its credit." (R. 346)

Under paragraph "3", (R. 347) the Secretary of Agriculture, with regard to the formation of a new loan company says:

"As soon as sufficient capital is assured, the organizers should get in touch with the Federal intermediate credit bank of the district. That bank will gladly give advice on the organization and operation of the corporation and provide samples of the necessary legal forms." (R. 348)

Again the Secretary says, in paragraph "4" (R. 348)

“The corporations (the loan company) income will be limited to a 2 per cent ($2\frac{1}{2}\%$ on livestock paper) spread in interest between the rate it charges its borrowers and the rate it pays the Federal intermediate credit banks. Experience shows that this income in many cases has been insufficient to pay expenses; and seldom, if ever, has been great enough to absorb large losses on loans.”

Again in paragraph “5”:

“Representatives of the group should get in touch with the State advisory committee as soon as possible after sufficient capital has been subscribed. That committee will advise the representatives as to the conditions which must be met to enable individuals to obtain loans to purchase stock of the corporation and will provide the necessary forms to make application.” (R. 348)

And in paragraph “6”:

“As far as possible, all applications for loans to purchase stock of a corporation should be forwarded to the State advisory committee in a group. This applies not only to new corporations in process of formation but to existing corporations whose capital is to be increased or reconstituted.” (R. 349)

In paragraph IV (R. 349) full details of instructions are given as to the execution of the various documents required for a loan, which consists of:

- 1st. The application;
- 2nd. Applicant's financial statement;
- 3rd. The note;
- 4th. The assignment of the stock to be purchased
(R. 350);

The additional forms are of especial interest in the case:

The fifth form is a Power of Attorney. As to this, the Secretary says:

“This paper when properly prepared will give to member of the State advisory committee the power to receive, indorse, and collect the check made out to you. Instructions on the reverse side should be read and the paper acknowledged before a notary public or other officer authorized to administer oaths.” (R. 351).

The sixth and last form is one of the most important. As to this the Secretary says:

“The sixth form to be prepared and signed is a letter of authority to the member of the State advisory committee named in the power of attorney to deliver your funds to such parties as the Secretary of Agriculture or his representative may direct.” (R. 351)

This procedure was faithfully carried out in the Bu-
leigh case. The documents are in evidence as exhibits, as follows:

Application (R. 121)

Applicant's financial statement (R. 147)

Burleigh's Note (R. 165)

Assignment of stock (R. 130)

Power of Attorney (R. 141)

Letter of Authority (R. 154)

Plaintiff's Ex. 5, which is the Letter of Authority (R. 154) authorized A. R. Altermatt (member of the State advisory committee) holding a Power of Attorney from Burleigh, to receive, endorse and collect United States Treasury check, payable to Burleigh as the proceeds of a loan for one or more of the purposes enumerated under Public Act. No. 666, and

“to transmit such check after endorsement by him, pursuant to the power of attorney above mentioned, and/or to pay over the proceeds thereof, to such person or persons as may be designated by the Secretary of Agriculture or his authorized representative.”

The proceeds of Mr. Burleigh's loan never came to Mr. Burleigh nor to the loan company (R. 181) but was sent to the bank to bolster up and make good bad loans the bank had received from the loan company (R. 182), which loans were prior to the Burleigh transaction. Mr.

Altermatt was selected by the Secretary of Agriculture (R. 183) and was never known by Mr. Burleigh.

The proceeds of the Burleigh loan, as well as that of the others similarly situated, were received by the bank as evidenced by the bank's acknowledgement dated June 1, 1931 (def. Ex. 17, R. 249). Under date of June 16, 1931, the bank wrote Curtice H. Martin, President of the loan company (def. Ex. 17, R. 251) concerning the cash received from the Burleigh matter and other similar transactions. In this letter it is stated that when the transaction is closed it will bring in \$37,700 and then states:

“The bank feels that the proceeds of these loans should be invested in liquid securities such as Federal Land Bank or Liberty Bonds to be held as excess collateral to your discounts and we shall appreciate your advising us which bonds you desire purchased and after the transaction has been completed, we will forward you our usual receipt.” (R. 252)

Mr. Warren, now President of the loan company testified (R. 253) that after the bank received the money detailed in Ex. 17 (R. 250), the bank invested this money in bonds and held the bonds; that the loan company never had the bonds or the proceeds of the Burleigh loan, but that the bank held the bonds under a receipt. As to why the bonds were held, he said:

“They are held for the purpose of securing any losses which may develop on their rediscounted line as additional collateral, known as additional collateral.”

He also testified that the bank collected the interest on the bonds and kept it, crediting the amount as cash collateral in the additional collateral account.

Financial statement identified by John M. Warren, resident. (R. 285)

The findings of fact embrace many of the details included in this statement (R. 77-111). Particular reference is made to findings 5 (R. 89), 6 (R. 91), 8 (R. 104), 10 (R. 106), 11 (R. 107-8), 12 (R. 109) and 13 (R. 110), in which, among other things, the court found (R. 104) that the plaintiff, through the Secretary of Agriculture, and those representing him, and the bank and the loan company, cooperating together, devised the plan for the sale of the Class “A” preferred stock at par, at a time when the corporation was purchasing its own stock from its stockholders at 75% of par; that the stock was represented as being worth par, and a good investment, and that these representations were made to Burleigh, among others, and that it was a good and desirable investment and the defendant did not know, and did not have the means of knowing

whether or not said representations were true; that the defendant was further told that the loan company was sound solvent and prosperous, and that the defendant believed these representations, and believing the same executed the note in evidence as Exhibit 10. (R. 105-106) Further it was found that said representations which materially influenced the defendant in signing said note were wholly untrue, and in particular it was found that at least \$50,000 of the capital of the proposed loan company was worthless and that in addition thereto it carried as assets other notes and properties which were worth substantially less than the amount at which they were carried, with the result that said Class "A" preferred stock at said time was worth practically nothing, and at the time of the trial was of practically no value. (R. 106)

The court further found that the plaintiff was fully advised of the exact condition of the affairs of the loan company at the time it entered into said plan, and it was never intended by the plaintiff, or the bank that any proceeds from the loan to Burleigh, or any other person similarly situated should get into the hands or possession of the loan company, nor under its control, nor be the basis for any additional or new loans, but that said plan was assigned for the sole purpose of benefitting said bank, and that the proceeds of said loan to the defendant, and others, should be held by the bank as additional security for money

ready due and owing to the bank on obligations in existence at the time said plan was initiated and carried into effect.

It was further found that it was no part of said plan that defendant or any other person similarly situated should procure the proceeds of his loan, or that the same should come into his possession or control, and to insure the plaintiff would never lose possession of, or dominion over the loan to the defendant, the Secretary of Agriculture, representing the plaintiff, appointed A. R. Altermatt as the active representative in Oregon of the plaintiff; (R. 107) that as a part of said plan, defendant executed the Power of Attorney authorizing A. R. Altermatt to endorse the government check whereby he supposed the loan would be consummated and that the "Letter of Authority" authorizing A. R. Altermatt to pay over the proceeds to such person or persons as might be designated by the Secretary of Agriculture, or his authorized agent, was a part of said plan, and that Mr. Altermatt executed the commission and consummated the plan by paying said money over to the bank, whereupon it was credited to the security account of the loan company, and by that governmental agency was invested in bonds, which were then and at all times since have been held as security for money then and theretofore loaned by the bank to the loan company. (R. 108)

It was further found that the loan company promised to redeem the stock at par with accrued dividends after two years from its issuance, provided the defendant, in the meantime, had paid up his loan; and it was further found that the defendant had paid up all of his indebtedness to the loan company and that it was within the power of the plaintiff and the loan company to carry said agreement into effect, and that it was the duty of the plaintiff and the loan company to surrender to defendant Burleigh his note and carry on such further transactions between themselves as will best serve their purposes.

It was further found that neither plaintiff nor anyone on its behalf, either paid or gave any consideration of any kind for the original note of the defendant, or for the renewal, and that neither the defendant nor anyone else received any benefit or consideration on account of the defendant signing it, and that the defendant would not have signed the note, nor any of the documents executed therewith, except on the belief on his part of various representations found in the findings to have been made to Burleigh and which he believed.

It was further found that the interest paid on the original note (Ex. 10) was paid by the loan company, which was in accordance with the promise made to the defendant by the loan company. (R. 108-109)

It was further found that prior to the execution of

note, and as a part of said plan, the defendant was advised that said note would be renewed and that acting in the belief that said transaction was genuine, and bona fide, and as represented to him, he executed the renewal note, shown as Ex. 1 herein.

It was further found that the defendant had no knowledge or means of acquiring the knowledge that the representations made to him at the initiation of said plan, were untrue, and the defendant still believed said representations to be true at the time of renewing said note, and acting in said belief signed said renewal note, but there was never any consideration given, nor received, for said note. (p. 110)

ARGUMENT

In the transactions out of which this litigation arose, plaintiff was represented by the Secretary of Agriculture, the bank, its examiners and officers and Mr. A. R. Aermatt, a member of the Advisory Committee for Oregon, appointed by the Secretary of Agriculture.

The loan company, as early as March 31, 1931, had liquidated its paper with the bank to the extent of \$630,187.6. (R. 287)

Based upon the examination of the loan company by the examiners of the bank on April 25, 1931 (R. 243) facts

developed which occasioned the bank to write, through manager, to the loan company (Def. Ex. 12, R. 208) a letter criticizing assets of the loan company carried on its books at \$50,935.73, which reduced the unimpaired capital to \$47,907.58. Of the loans which the loan company had rediscounted with the bank \$48,730.59 were listed as "fair" and \$40,730.59 as "doubtful" (R. 219). In addition to the above, unpledged assets of the loan company were listed as "fair" to the extent of \$19,769.38 and \$40,000.00 as "doubtful." (R. 220)

In this letter from its manager, the bank criticized the excessive loan value at which cattle were being carried on the security for rediscounted paper (R. 212). It also criticized the excess loans which had been rediscounted. (R. 211)

With the loan company's capital thus impaired, and while under the extreme pressure from the bank, as evidenced by the above letter from Mr. Meyer (R. 208), the loan company attempted to repair its capital structure by the sale of its 6% "A" preferred stock, first to its borrowers, and second, to the public. It represented to the defendant Burleigh that it (the loan company) was in sound financial condition, and that this stock would be a good investment. It requested its borrowers to take stock at least to a 10% of their loans, and recommended that they take larger amounts because of the desirable investment features. (R. 172, R. 176-7-8-9)

In his application for the loan (R. 127) it was expressly stipulated that the loan was desired "for the purpose of increasing the capital stock of the loan company" (R. 128). This was in line with the letter from the loan company to Burleigh (R. 172). Among other things, it is stated in this letter:

"The money the Government will advance to increase our capital will enable us to further serve the stockmen in our territory."

From March 31, 1931, to Oct. 31, 1931, the outstanding "A" preferred stock of the loan company never changed from \$50,000 (R. 286-295), although the bank received from the plaintiff on the loans to Burleigh and others \$34,700, representing loans to the individuals listed, the proceeds of which "have been used to purchase stock in the Agricultural & Livestock Credit Corporation." (R. 25)

Instead of selling out of its treasury \$34,700 worth of "A" preferred stock, and thereby increasing its capital to the extent of \$34,700 (in accordance with the representations to Burleigh) the old stockholders sold their "A" preferred stock to the corporation, which, in turn, sold the same stock to Burleigh and others. The old stockholders sold their stock back to the corporation at 75% of par, and were authorized to use the credit in purchasing 8%

"B" preferred stock at par (R. 390). The company also purchased 100 shares of the "A" preferred stock from its debtor and affiliate, Portland Livestock Co. at 75% of par (R. 390, 395). What became of the proceeds of the "A" stock which the company purchased from its stockholders is not disclosed by this record, but it is obvious that it was not all used for the purchase of the "B" preferred stock. This statement is based upon the financial statements of the company submitted to the bank March 31, 1931, to and including Oct. 31, 1931, (R. 286-291) which discloses that on March 31 the outstanding "A" preferred stock was \$32,750, and on April 30 was \$42,200, and this amount was not thereafter changed.

From the minutes of a directors' meeting of January 12, 1932, we glean the following interesting statement (R. 394-395):

"The secretary reported that under resolution authorizing purchase of Class "A" preferred stock at \$30 per share, the holders of such stock have sold this corporation 290 shares, and that all of such shares, together with 100 shares accepted from the Portland Livestock Company, and 40 shares heretofore purchased, have been sold at par to persons securing loans from the United States Department of Agriculture."

It is interesting to note that the letter from the company to Burleigh is dated March 19, 1931 (R. 12

and the minutes of the directors' meeting which made provision for taking back stock already outstanding are dated April 13, 1931.

The plaintiff paid its money over to its agent, the bank, and its receipt was acknowledged on June 15, 1931. (R. 249)

On June 22, 1931, (R. 391-394) the directors met and charged to Profit and Loss \$15,107.79 of assets carried at par at the time Burleigh and the others were solicited to buy the "A" preferred stock.

These minutes disclose that \$10,950 had been released through the exchange of Class "A" preferred for Class "B" preferred, which amount was credited to Reserve for Losses. This entry simply means that the old stockholders turned in their "A" preferred stock, which was of practically no value, as disclosed by the criticisms of the Manager and Assistant Manager of the bank (R. 208, R. 227), and the report of the bank's examiners (R. 214, R. 220, R. 233, and R. 239) and the charges to Profit and Loss made by the directors of items under criticism at the time the stock was sold to Burleigh as disclosed by the minutes of the corporation (Def. Ex. 25, R. 392, 393, 396, 397, 398, R. 310, 311, 312, 313, 314 and 315).

The Secretary of Agriculture proposed to loan money to increase the capital of the loan company. Burleigh and

the others proposed to buy new stock, and thereby increase the capital of the loan company, and, in turn, make it possible to better serve the livestock industry.

The bank was dissatisfied with the status of its red-accounts from the loan company. The bank's officers challenged the solvency of the loan company, both before the loans were made (R. 208) and in October and December, 1931, after the loans were made (R. 227). If the capital structure of the loan company was sound and represented sound assets, there would have been no occasion for the original stockholders to turn over stock into the corporation at 75% of par, and in turn sell it to Burleigh and others at par.

If the Secretary of Agriculture had believed that the loan company was solvent he would have directed Mr. Termatt to pay the proceeds of the Burleigh and other loans to the loan company in payment for its new stock issued and sold, as Burleigh and the others believed was being done.

Instead of introducing new capital stock into the loan company so that it could better serve the livestock industry, the Secretary of Agriculture took the plaintiff's money out of the left pocket (the Treasury of the United States) and put it over in its right pocket (the bank at Spokane), which was a part of the plan of the Secretary of Agriculture to improve the status of the Federal Bank.

Spokane by getting additional cash into the hands of the bank as additional security for money already loaned to the loan company in the way of rediscounting livestock paper at the bank considered of a value less than the amount that had been advanced. The Secretary of Agriculture described the bank when he stated (R. 346):

“The Federal intermediate credit system which discounts the notes of such corporations, can accept only such paper as is described in the law governing their operations. That system is not an emergency institution. It is a permanent organization which like any other banking system must protect its credit.”

In the formation of a new agricultural credit loan company the Secretary of Agriculture instructed as follows (L. 347):

“As soon as sufficient capital is assured, the organizers should get in touch with the Federal intermediate credit bank of the district. That bank will gladly give advice on the organization and operation of the corporation, and provide samples of the necessary legal forms.” (R. 348)

It is further directed that “representatives of the group should get in touch with the State Advisory Committee as soon as possible after sufficient capital had been subscribed.” (R. 348).

In this document the Secretary of Agriculture outlined

each step to be followed in procuring a loan either to form a new loan company, or to provide additional capital, or to repair the capital of an existing company (R. 351). The sixth form is of especial interest for by this "Letter of Authority" the United States, acting through its Secretary of Agriculture, and his representatives, kept complete control over the proceeds of these loans at all times.

Mr. Burleigh executed this Letter of Authority, in which, authority was given to Mr. Altermatt, the agent of the Secretary of Agriculture and member of the State Advisory Committee, to transmit the treasury check, after endorsement by him, and to pay over the proceeds thereof to such person or persons as may be designated by the Secretary of Agriculture, or his authorized representative (R. 154). That Mr. Altermatt executed this authority and delivered the proceeds of Burleigh's loan to the banks is evidenced by Def. Ex. 17 (R. 249-252)

The story is now complete. Burleigh was told that the company's "A" preferred stock would be a good investment; that he would never have to pay the note (R. 17); that by buying this stock he would add new capital to the loan company, and thereby enable it, at the ratio of ten to one, to better serve the livestock industry.

The Secretary of Agriculture furnished a complete printed set of instructions for the consummation of the loan to increase the capital of this corporation. The application

tion specifically states that it is to increase the stock of the company. The plaintiff, through its agent (the bank) knew that the stock of the company was of impaired value. Its examiners examined the minute books of the loan company and knew, or should have known, that no new stock was being sold (R. 231).

The financial statements, which are in evidence (R. 23 et seq.) are copies of statements made by the loan company to the bank (R. 300). They disclose that no addition had been made to the capital except \$7500 to the "B" stock.

The Secretary of Agriculture never lost control of the Burleigh loan. He had Burleigh's note, the unendorsed stock certificate and, through his agent, had the proceeds of the loan, and sent it to the government's bank at Spokane, which bank kept all of the money and invested it in bonds and kept the principal and interest paid thereon up to the time of the trial. (R. 249, 297-8)

Burleigh received nothing (R. 163), and the plaintiff gave nothing for the note which is before this court at this time. The Government owns the bank, and the proceeds of Burleigh's loan were turned over to the Government, through its bank, to be held as additional collateral security (R. 249, 297, 298). To collect the Burleigh note is to consummate the fraud which was initiated at the beginning of his entire transaction. The whole purpose of the trans-

action was to build up the impaired capital of the loan company for the benefit of the plaintiff, through its ownership of the bank. If the transaction herein delineated had been inspired and carried out by private individuals, and the mails of the United States had been used in connection therewith, it certainly would have been a suitable case for prosecution for use of the mails in consummation of a fraudulent scheme.

The bank is a Federal Intermediate Credit Bank formed by the plaintiff under authority of Acts of Congress. Its stock is wholly owned by the plaintiff. (12 U. S. C. A. 1061).

Such banks, while governmental agencies, have the power to sue and be sued. (12 U. S. C. A. 1023).

The Farm Credit Administration is authorized to grant charters for twelve Federal Intermediate Credit Banks of which the Spokane bank is one. (12 U. S. C. A. 1020)

The directors of the several Federal Land Banks are ex-officio the directors of the several Federal Intermediate Credit Banks, and these directors are, subject to the approval of the Governor of the Farm Credit Administration, authorized to employ and fix compensation of such officers and employees of the Federal Intermediate Credit Banks as may be necessary to carry on the business authorized by sub-chapter 3, chapter 7, 12 U. S. C. A.

At the request of counsel for plaintiff it was stipulated that the Farm Credit Administration is a legally constituted agency of the United States of America, vested with the duties and authority incident to the administration of the agricultural credit system of the United States. (R. 12-123)

We have never doubted that the Farm Credit Administration and its Governor, and all of the Federal Intermediate Credit Banks are governmental agencies and instrumentalities created by Act of Congress, and administered under these laws and lawfully made executive orders, and that the Federal Intermediate Credit Bank of Spokane is as much an agent of the plaintiff as the Secretary of Agriculture, or any other Federal official, institution or agent, acting in their several capacities and realms of activity.

A number of times throughout the trial, counsel for the plaintiff indicated the belief that the United States of America was acting in its sovereign capacity, could not be liable for a fraudulent transaction, and could not be held responsible for the acts of its agents.

However, the Supreme Court, as well as several of the Courts of Appeal, and District Courts have, in well-considered opinions, directly held to the contrary of counsel's contention.

One of the earlier cases was *United States vs. The State Nat. Bank of Boston*, 96 U. S. 30, 36, 24 L. Ed. 647, 61. After holding that the sovereignty of the United States was not involved in similar questions, the court said:

“But surely it ought to require neither argument nor authority to support the proposition, that, when the money or property of an innocent person has gone into the coffers of the nation by means of a fraud of which its agent was a party, such money or property cannot be held by the United States against the claim of the wronged or injured party.

“The agent was agent for no such purpose. His doings were vitiated by the underlying dishonesty, and could confer no rights upon his principal.

“The appellee recovered, below, the amount claimed. A different result here would be a reproach of our jurisprudence.”

Where the United States elects to become party to commercial paper, it assumes all responsibilities of private persons under the same circumstances. (*U. S. vs. National Exchange Bank of Baltimore*. (C. C. A. 4th Circuit) 1 Fed. (2d Series) 888, 890. Affirmed 270 U. S. 70 Law. Ed. 718.)

In discussing the question of whether it is practically impractical for the Federal Government to conduct

business, and, at the same time, be responsible for the multitude of clerks handling its business, the Circuit Court of Appeals used the following language:

“It (the United States) asks, is it reasonable to suppose that everyone of those whom it charges with the duty of paying its obligations can know the amount for which each of them was in the first instance drawn?

“It is not for us to say whether the business of making such payments can be so organized, distributed, and safeguarded as to insure that he who pays may surely and swiftly ascertain for what sum the check or draft was issued. It is enough that, when the United States elects to become a party to commercial paper, it assumes all the responsibilities of private persons under the same circumstances. *Cook v. United States*, 91 U. S. 389, 23 Law Ed. 237; *U. S. vs. Bank of New York National Banking Association*, 219 Fed. 648, 134 C. C. A. 579, L. R. A. 1915 D 797. If the burden becomes too heavy, Congress can give relief.”

In affirming this decision, the Supreme Court, speaking through Justice Holmes, 270 U. S. 534, says:

“If the drawer and the drawee are the same, the drawer cannot recover for an overpayment to an innocent payee because he is bound to know his own checks. * * * In this case there is no doubt that in truth the check was drawn by the United States upon itself.

“The government attempts to escape from this conclusion by the fact that the hand that drew and the hand that was to pay were not the same. * * * The United States does business on business terms. *Cook v. United*

States, 91 U. S. 389, 23 L. Ed. 237. * * * We are of the opinion that the United States is not excepted from the general rule by the largeness of its dealings and having to employ agents to do what if done by a principal in person would leave no room for doubt."

While it is true that "aches is not imputable to the government, in its character as sovereign, by those subjected to its dominion," it is equally true that "if it comes down from its position of sovereignty, and enters the domain of commerce, it submits itself to the same laws that govern individuals there." *Cook et al vs. United States*, 91 U. S. 389, 398, 23 L. Ed. 237. *United States vs. National City Bank of New York*, 28 Fed. Supp. 144, 150, 151.

In *Keifer & Keifer v. Reconstruction Finance Corporation*, 83 L. Ed. 512, the Supreme Court in a decision handed down February 27, 1939, held that the Government does not become the conduit of its immunity in suits against its agents or instrumentalities merely because they do its work.

This case would appear to be of special interest as it arose under the statute which, in its amended form, is now by authority of Executive Order No. 6084, is now the statute under which the Federal Intermediate Credit Bank operates. The authority of the Reconstruction Finance

Corporation, by the above executive order, has been transferred to the Farm Credit Administration. We do not have the paging of this decision in the U. S. Reports.

In *United States vs. Standard Oil Co. of California*, 21 Fed. Supp. 645, 655, it is said:

“With all due regard for the powers and attributes of sovereignty, it is well to remember that, when a sovereign comes into a court of equity seeking its aid to enforce its rights, even as the owner of the public domain, its claim should be tested by the same equitable principles which govern suits between private litigants, unless there be a special statute commanding a contrary rule. See *United States v. Stinson*, 1905, 197 U. S. 200, 25 S. Ct. 426, 49 L. Ed. 724; *United States v. Debell*, C. C. A. 1915, 227 F. 775. As said by the Supreme Court in a very recent case, *American Propellor & Mfg. Co. v. United States*, 1937, 300 U. S. 475, 478, 57 S. Ct. 521, 523, 81 L. Ed. 751: ‘We have said (*United States v. The Thekla*, 266 U. S. 328, 339, 340, 341, 45 S. Ct. 112, 113, 69 L. Ed. 313): ‘When the United States comes into Court to assert a claim it so far takes the position of a private suitor as to agree by implication that justice may be done with regard to the subject-matter. The absence of legal liability in a case where out for its sovereignty it would be liable does not destroy the justice of the claim against it. * * * The reasons are strong for not obstructing the application of natural justice against the Government by technical formulas when justice can be done without endangering any public interest.’” Affirmed (C. C. A. 9th Circuit) Nov. 16, 1939.

Our suggestion that the plan which was carried out in this case, and the use of the mails in connection therewith, would have constituted an indictable offense for using the mails to effect a fraud, is supported by the language of 18 U. S. C. A. Sec. 338, Note 31, and the cases therein cited. *Wilson vs. United States*, 190 Fed. 423, 432-43, and *Meyers vs. United States*, 223 Fed. 919, 925, are conclusive of this proposition.

In both of these cases the fraud in part consisted in representing that the corporate stock which was being sold was treasury stock, and that the proceeds thereof would go into the treasury of the company, whereas, in fact, the stock which was sold had already been issued and was outstanding, and was taken in and resold, with the proceeds going to the former owners.

Burleigh was not only interested in buying a sound security in a solvent company, which stock was worth at least par, but he was also interested in the representation that by buying this stock the capital of the loan company would be increased, and thereby its ability to serve the livestock industry would be increased ten-fold.

The records of the corporation disclose that no material representation made to Burleigh was true, but that most thereof was false, as follows:

- (a) The Government, in fact, made no loan either

Burleigh, or to the loan company. It merely went through the form of making a loan.

(b) The Government never parted with control of the money it purported to loan Burleigh, but through its agent, Mr. Altermatt, kept control of the money and diverted it into its own coffers at the bank at Spokane.

(c) The amount of the outstanding "A" preferred stock of the loan company was never increased one share; its "B" stock appears to have been increased \$7500 in April (R. 287, 288), whereas the loan company had no notice that the bank had received any of this money until June 15 (R. 249), at which time it was advised by the bank that it had received checks from the Treasury of the United States amounting to \$34,700, representing loans to the individuals listed thereon "the proceeds of which have been used to purchase stock in the Agricultural & Livestock Credit Corporation."

(d) The stock was not worth par, as evidenced by the willingness of the persons who owned it to surrender it at 75 on the dollar to the corporation, and that the Portland Livestock Co. would surrender its "A" preferred stock at 75 of par to be credited on the money owed the loan company. (Directors' meetings Apr. 13, 1931, R. 389.)

(e) The impairment of capital of the loan company is further established by the criticisms of the plaintiff's agent,

the bank's examiners, and manager (R. 208, R. 227), and the capital items at that time criticized, which were charged off by the directors and stockholders thereafter (R. 30, 311, 391, 392, 393, 394, 396, 397, 398, 399, 400, 409).

(f) After the bank had received \$34,700 from the Treasurer of the United States on account of loans made to individuals for the purchase of stock in the loan company the plaintiff, through its bank again examined the loan company on October 29, 1931, (R. 227) and in discussing certain capital paper of the loan company which had been criticized in April, at the time the loan company was selling its stock to Burleigh, the Assistant Manager of the bank denominated \$37,365.38 of this previously criticized paper as "worthless" (R. 229).

(g) No word short of "fraud" could describe the result of the plan which was worked out, and to which the defendant, through his lack of knowledge or ability to acquire knowledge, innocently became a victim.

It is not necessary to burden this brief, or the court with legal definitions of "fraud" in order to establish that the entire plan was fraudulent, and the plaintiff and the loan company used the defendant as a means of accomplishing the end they had in mind, to wit: to make the records of the bank, representing its dealings with the loan company, appear more satisfactory.

At the conclusion of the trial, His Honor, the Trial Judge, indicated his conviction as to how this entire matter should be closed out (R. 374-379).

The findings of fact made by the trial court leave no doubt that the plaintiff cannot recover in this action, and that it should surrender the note to the defendant, the stock certificate to the loan company, and permit the bank to carry on its relationship with the loan company according to its own ideas, limited by its contractual obligations.

If the loan company is solvent, it can, and no doubt will, pay its obligations to the bank, whereupon neither the plaintiff nor the bank will be further interested in the loan company.

To permit the plaintiff to recover in this case is to compel Burleigh to pay for stock of the loan company which was not treasury stock, which was of small or no value in April, 1931, and of nominal (if any) value now.

Burleigh has paid his loan to the loan company, and, as an inducement to purchase the stock, he was promised that when he paid this loan the loan company would redeem the stock at par and pay the note to the Government. The loan company is a guarantor of the Burleigh note; its obligations to the bank are recognized and unquestioned, and, as stated, if the loan company is solvent, it can and will discharge its debts to the bank.

By bringing this action, the plaintiff is endeavoring to accomplish the final chapter in a transaction reeking with fraud at its inception, and to compel the one innocent party to the transaction, the defendant, to suffer the financial losses which would result if this fraudulent transaction now to be consummated.

Respectfully submitted,

BURLEIGH & BURLEIGH,

J. A. BURLEIGH,

JAY BOWERMAN,

Attorneys for Appellee.